STATE OF CONNECTICUT
DEPARTMENT OF PUBLIC UTILITY CONTROL

JACK R. GOLDBERG
Commissioner

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In The Matter Of: Petition of LCI Corporation for Declaratory Ruling

Common Carrier Docket 98-5

In the above docket, the attached letter has been sent to the following members of the Federal Communications Commission:

William Kennard, Chairman
Susan Ness, Commissioner
Gloria Tristani, Commissioner
Michael Powell, Commissioner
Harold Furtchgott-Roth, Commissioner
Office of the Secretary, Magalie Salas, Secretary

Dated at New Britain, Connecticut, this 11th day of March, 1998.

Jack R. Goldberg

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DEPARTMENT OF PUBLIC UTILITY CONTROL

JACK R. GOLDBERG
Commissioner

March 11, 1998

The Honorable William Kennard, Chairman
Federal Communications Commission
1919 M Street, N.W.
Washington, D.C. 20554

Dear Chairman Kennard:

In response to the discussions that took place in the Communications Committee meetings at the NARUC Winter Conference in Washington, D.C., I am convinced that there is a significant amount of confusion concerning the LCI petition filed with the FCC concerning a model for LEC wholesale/retail operational separation. I participated as a member of the Connecticut DPUC panel that investigated and subsequently approved the wholesale/retail separation for the Southern New England Telephone Company in June 1997. I would like to point out several differences between the SNET decision and the LCI proposal, differences that I believe severely limit both the utility of the LCI model for the BOCs and the probability the BOCs would accept this model as a Section 271 "condition".

One of the most significant distinctions is the requirement in the LCI proposal (Page 17) for a minimum of 40% public ownership of the retail operation arm of the BOC (ServeCo). Although LCI is careful to note that this must be a voluntary concession by a BOC, LCI has never addressed the effect on shareholders that the 40% ownership shift will have. The tax effects of public ownership of 40% are extremely significant. Consolidated tax filings would no longer be permitted and ServeCo would now face a 34% federal tax on net income in addition to the same tax rate on any retail earnings that flow up to the parent holding company (HoldCo).

An examination of a hypothetical case is quite instructive. In fiscal year 1996, Bell Atlantic (pre-merger) had net income of $1.88 billion. If we assume that 40% of this income was generated by activities that would comprise ServeCo after the split, this would indicate an additional $752 million penalty just for a change in the structure of the

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corporation. Remember that the HoldCo is still doing exactly the same business, just under a different corporate structure. A very stiff penalty, to be sure.

The proposal concerning directors (Page 17 and footnote 23) is not completely clear, but it seems to indicate that ServeCo directors could have "no financial interest in NetCo or HoldCo (including stock ownership)...". Since the proposal allows HoldCo to have as much as 60% ownership in ServeCo, it is difficult to envision how a board of directors could meet its fiduciary responsibilities over a subsidiary business unit in which it has no board seats. Most holding companies have a requirement that their board members own stock, immediately disqualifying them from a seat on ServeCo, even though they represent the majority owner. This would likely lead to shareholder suits concerning the performance of directors and management.

Further, on Page 18, the proposal requires the application of Section 272 separation requirements in addition to the two unique provisions noted above. If actual public ownership and partial divestiture are present to "...ensure that it [ServeCo] has a significant fiduciary obligation other than to HoldCo.", then why are Section 272 rules necessary? If this is supposed to be a viable proposal it cannot be loaded with so many rules and prohibitions that it never gets serious consideration by a BOC.

The LCI proposal places no finite end point on the provision of retail service by NetCo. Until NetCo withdraws completely from the retail service market, its retail presence creates an untenable conflict between NetCo and ServeCo, both serving the same retail market. In order for this proposal to work a specific deadline or condition must be set for NetCo to cease all retail services.

Also on Page 18, NetCo is required to maintain ownership and control of an extensive list of assets, including billing and collection. By definition NetCo will not provide retail service. Why are they required to keep (and not share) billing and collection when ServeCo is the entity which will be providing retail service and need those specific functions?

Finally, the LCI proposal requires that the Operational Support Systems be capable of supporting ordering activities volumes and time frames equivalent to those offered by the BOC for Preferred Interstate Carrier (PIC) changes. A PIC change is generally handled in 24 - 48 hour time frames with little or no manual intervention. Even internally within a BOC, using its own systems, a new installation order or service change is seldom if ever met in that time frame today. How, and why, would any BOC develop a system capable of satisfying the LCI desired level of performance short of being ordered to do so, and even then who would pay for its development? There is no evidence that local service changes and churn will approach the levels seen in the long distance industry. The resources wasted in this massive development are not economically justified by any analysis.

The SNET separation decision accomplished the same ends as the LCI proposal with far fewer conditions that could be deemed controversial or contestable. Furthermore, the SNET model goes a step further in providing the public an opportunity to participate in the market restructuring by requiring a ballot of all customers to ensure the end of NetCo supplying retail service. LCI's proposal has earned a significant amount of discussion, but the specific details encompassed are, in my view, fatal to any effective implementation of a wholesale/retail split and a "Fast Track" Section 271 approval for any BOC.

I would be happy to discuss any of these issues in depth if you care to do so.

Sincerely,

Jack R. Goldberg
Commissioner